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Washington State SCS Senate Committee SERVICES

SUMMARY OF INITIATIVE 747 TO THE PEOPLE

(Limiting Property Tax Increases)

This information has been prepared in response to various requests for a summary of the provisions of Initiative 747, which will be before the voters at the statewide general election on November 6, 2001. The material in this summary is provided for informational purposes only. It is provided for use by members of the Legislature and legislative staff. It is not provided as an expression for or against any of the provisions of Initiative 747.

BRIEF SUMMARY

Currently, the annual growth of regular property tax levies for each taxing district is limited. For most districts, the allowable annual growth is inflation, as measured by the implicit price deflator (IPD). Taxing districts may raise their property tax levies more than inflation (up to six percent) with a vote of the district's governing body. Small property taxing districts (less than 10,000 in population) are allowed to grow by six percent per year without a special vote.

Initiative 747 changes the growth limit for small districts to one percent per year and to the lesser of one percent or inflation for all other districts.

In total, the growth in regular property taxes paid by taxpayers will be less with the passage of the initiative. On average, regular property tax levies will increase by one percent per year. However, individual property owners will see property tax increases greater or less than one percent per year depending upon individual circumstances. Additionally, the initiative does not limit voter-approved levies and it does not limit the growth in the assessed value of property.

BACKGROUND

Property taxes in Washington will generate $5.7 billion in calendar year (CY) 2001. The property tax is the third-largest source of revenue to the state general fund, generating approximately $1.4 billion in CY 2001. The state property tax is often referred to as the “state school levy” because it is dedicated solely for the support of public schools. The property tax is the single largest source of revenue for local governments in Washington state, generating about $2.5 billion per year and representing about 48 percent of all local government tax revenues. "Special" school levies comprise the remaining $1.8 billion.

Under current law, the growth of regular property tax levies is limited each year. The limit is an amount calculated by multiplying the taxing district’s highest levy during the three preceding years by the percentage increase in the implicit price deflator (IPD) as published for the most recent 12-

month period in September of the year before the taxes are due, plus a component for new construction. In calendar year (2001), IPD is estimated by the Office of the Forecast Council to be 2.1 percent.

- The percentage is six percent for a taxing district of less than 10,000 in population and is the lesser of six percent or inflation for all other taxing districts.
- Taxing districts may increase this percentage up to six percent for the year by a special vote of its legislative body. In districts with legislative authorities of four members or less, two-thirds of the members must approve such increases. In districts with more than four members, a majority plus one vote is required.
- The component for new construction is equal to the amount of revenue that the value of new construction in the district would have generated at the preceding year's tax rate.

Any levy by a taxing district in excess of the taxing district's limit requires voter approval. If such a levy is approved, it becomes the base for calculation of future levies, unless approved for a limited time or purpose.

The property tax growth limit applies to the regular (non-voter-approved) levies of each property taxing district. This includes the state, counties, cities, port districts, fire protection districts, library districts, metropolitan park districts, public hospital districts, and other taxing districts. The limit does not apply to excess or so-called "voter-approved" levies such as local school maintenance and operation levies and levies to retire bond issues.

The limit is a restriction on total property taxes that may be levied by a <u>district</u>. It does not limit the growth in the assessed value of a particular parcel of property nor does it limit the growth in property taxes on a parcel of property. If a local assessor determines that the value of a parcel of property should double in value (as determined by the market), the tax on that property will double even if the district's <u>total</u> taxes increase by only a small amount.

When assessed values rise more quickly than the property tax growth limit, the effect of the limit is to lower the overall tax rate of the district. This is because as property values rise, a lower rate will generate the same amount of taxes. A six percent limit reduces the district's tax rate to a rate that would generate only six percent more revenue. Conversely, if assessed values are growing more slowly than the limit (less than six percent per year for a limit of six percent), a taxing district's tax rate must increase to generate six percent more revenues than the previous year. When the district reaches its statutory rate limit, the tax rate can no longer increase and the taxing district will collect less revenue than would be otherwise allowed.

The limit on regular property tax levies was originally enacted in 1971 with a limit on taxing district revenues equal to six percent, effective with taxes payable in 1974. The taxing district could also increase its levy by the value of new construction in the district multiplied by the previous year's tax rate. In 1970, the U.S. Consumer Price Index (CPI) was 5.9 percent. The limit allowed taxing districts to raise their levies sufficient to provide for increased service levels (roughly equivalent to the new construction component) and to pay for the increased costs of providing current services (roughly equivalent to the inflation component).

The six percent limit on regular property tax levies was significantly altered by the passage of Referendum 47, which was approved by the voters in 1997. That measure lowered the six percent limit for most taxing districts to what it is today under current law.

INITIATIVE 747

Initiative 747 reduces the annual property tax growth limit for a taxing district of less than 10,000 in population from six percent to one percent. For all other taxing districts with populations greater than 10,000, including the state, annual property tax levies are reduced from inflation (currently 2.1 percent), to the lesser of one percent or inflation as measured by IPD. If inflation is less than one percent, then a taxing district, other than the state, may provide for the use of a limit of up to one percent for that year with a vote of the legislative body of the district. In districts with legislative authorities of four members or less, two-thirds of the members must approve such increases. In districts with more than four members, a majority plus one vote is required. Initiative 747 does not change the requirement for voter approval of any levy in excess of the taxing district's limit.

FISCAL IMPACT ON TAXPAYERS

In each taxing district, the annual growth in regular property taxes will be less with the passage of the initiative. On average, regular property taxes will grow at the same rate as the new limit of one percent per year, and all taxpayers will pay less in regular property taxes than they would have paid under current law. However, as provided under current law, the regular property taxes of those taxpayers with assessed value growth faster than average will see tax increases faster than the overall growth limit. Conversely, owners of slow growing property will see increases less than the overall growth rate. Taxpayers will save almost $1.8 billion over the next seven years. Taxes will tend to increase on average, but at a slower rate than under current law.

Taxpayer Savings ($ Millions)
Reduction from Current Projected Property Tax Growth

	CY 2002	CY 2003	CY 2004	CY 2005	CY 2006	CY 2007
State Property Tax	$16.7	$34.5	$58.3	$83.5	$110.4	$147.6
Local Regular Taxes	$56.0	$115.3	$179.7	$248.1	$321.4	$404.2
Annual Total	**$72.7**	**$149.8**	**$238.0**	**$331.6**	**$431.8**	**$551.8**
Cumulative Savings	**$72.7**	**$222.5**	**$460.5**	**$792.1**	**$1,223.9**	**$1,775.7**
Estimates provided by the Department of Revenue - Research Division						

The initiative does not limit voter-approved levies. Therefore, the growth in all property taxes for a taxpayer in a district where a voter-approved levy is passed could exceed the limit because the limit is only on regular property tax levies.

The initiative also does not limit the growth in the assessed value of property. Constitutional questions have been raised when values are limited. This is not a consideration for this initiative. Because there is no change to values, there is no shift of taxes from one set of taxpayers to others.

FISCAL IMPACT ON STATE AND LOCAL GOVERNMENTS

State Impact

Based on analysis by the Department of Revenue, Initiative 747 would reduce state property tax collections by $16.7 million in calendar year (CY) 2002 growing to a total of $451 million over the next six calendar years. These reductions do not mean that the state property tax levy will not increase at all, merely that it will increase less than would have been the case if Initiative 747 were not enacted. In 2007, the state school levy would be reduced by about $148 million or eight percent from what it would have grown. This is a result of the growth in the state school levy being reduced from inflation to one percent.

State Property Tax Impact ($ Millions) Reduction from Current Projected Property Tax Growth						
	CY 2002	**CY 2003**	**CY 2004**	**CY 2005**	**CY 2006**	**CY 2007**
Annual	($16.7)	($34.5)	($58.3)	($83.5)	($110.4)	($147.6)
Cumulative	($16.7)	($51.2)	($109.5)	($193.1)	($303.5)	($451.2)
Estimates provided by the Department of Revenue - Research Division						

Property taxes are collected on a calendar year basis; however, governments operate on a fiscal year basis. For the state property tax, the fiscal year 2002 state impact is $8.5 million and the fiscal year 2003 impact is $25.9 million for a total of $34.5 million in reduced property tax revenues for the 2001-03 biennium. Put another way, the current state property tax would generate $2.899 billion in the 2001-03 biennium, but will only generate $2.865 billion if Initiative 747 passes. Over the next six years, the state property tax would generate $451 million less in revenue to the state general fund than it would have if Initiative 747 is enacted.

Local Impact

The initiative would reduce local taxing districts' property tax collections by $1.3 billion over the next six years. These reductions would result from local property tax levies increasing more slowly than they are currently projected to increase. In order to estimate these revenue reductions, it was necessary to project a baseline for future local levies under the current law. This analysis assumes that local districts would have continued to increase their levies by the same percent increase taken for taxes due in calendar year 2000. Therefore as a basis for this estimate, the districts growing six percent each year were assumed to continue to do so, those growing by inflation were assumed to continue, as were the districts that collected somewhere between the inflation and six percent. Of course, alternative assumptions about local district levy amounts would produce different fiscal impacts.

On average, 2007 property tax levies would be 12 percent lower with the passage of Initiative 747 than they otherwise would have been. Hospital districts, port districts, and metropolitan park districts would be affected more significantly, with the growth in property tax collections being reduced by more than 20 percent. While the growth of the state school levy and many local district levies would be reduced from about 2.1 percent (IPD inflation) to one percent, the growth of property tax levies for taxing districts under 10,000 in population would be reduced from six percent to one percent. Therefore, in percentage terms, the smallest taxing districts (and those larger districts that have voted to collect more than IPD) would be most affected. The table below depicts the estimated revenue reductions that would result from the passage of Initiative 747 by type of taxing district.

Local Impacts ($ Millions) Reduction from Current Projected Property Tax Growth						
District Name	**CY 2002**	**CY 2003**	**CY 2004**	**CY 2005**	**CY 2006**	**CY 2007**
County Current Expense	($9.8)	($20.4)	($32.6)	($45.8)	($59.7)	($76.1)
County Road	(6.7)	(13.9)	(22.3)	(30.8)	(40.0)	(50.2)
Cities	(19.9)	(41.3)	(63.7)	(86.3)	(109.9)	(136.6)
Libraries	(4.5)	(9.0)	(13.9)	(19.4)	(25.9)	(32.9)
Hospitals	(1.2)	(2.4)	(3.9)	(5.5)	(7.2)	(9.1)
Fire Districts	(7.4)	(15.0)	(23.2)	(31.7)	(40.7)	(50.7)
Metro Park	(0.3)	(0.7)	(1.1)	(1.5)	(2.0)	(2.5)
Emergency Medical	(2.1)	(4.0)	(6.6)	(9.3)	(12.1)	(15.6)
Ports	(3.8)	(7.6)	(11.8)	(16.4)	(21.5)	(26.9)
Other Districts	(0.4)	(1.0)	(0.7)	(1.3)	(2.4)	(3.6)
Annual Total	**($56.0)**	**($115.3)**	**($179.7)**	**($248.1)**	**($321.4)**	**($404.2)**
Cumulative Total	**($56.0)**	**($171.3)**	**($351.0)**	**($599.2)**	**($920.5)**	**($1,324.7)**
Estimates provided by the Department of Revenue - Research Division						

Another factor to be considered in assessing the overall fiscal effect of Initiative 747 is the relative importance of property taxes as a share of a taxing district's total revenues. Currently, 12.5 percent of the state general fund is derived from property taxes. For cities, the relative share is 20 percent and for counties it is 32 percent. Special districts are typically more dependent on property taxes. In some cases, such as library districts and fire districts, the only revenue source for the district is the property tax. For port districts, over 90 percent of their tax revenue comes from the property tax, but it represents only 10 percent of their overall revenue. This is because of port districts' ability to generate revenue from operations in addition to taxes.

For further information contact:
David Schumacher, (360) 786-7474
Terry Wilson, (360) 786-7433
Senate Ways & Means Committee